

VZCZCXRO6462
RR RUEHDA
DE RUEHAK #0346/01 0301635
ZNR UUUUU ZZH
R 301635Z JAN 06
FM AMEMBASSY ANKARA
TO RUEHC/SECSTATE WASHDC 2799
INFO RUEHDA/AMCONSUL ADANA 0335
RUEHIT/AMCONSUL ISTANBUL 9699
RUEATRS/DEPT OF TREASURY WASHDC

UNCLAS SECTION 01 OF 02 ANKARA 000346

SIPDIS

SENSITIVE
SIPDIS

TREASURY FOR CHRIS PLANTIER

E.O. 12958: N/A

TAGS: [EFIN](#) [TU](#)

SUBJECT: TURKEY CENTRAL BANKER WORRIED ABOUT BACKSLIDING

REF: ANKARA 40

11. (SBU) Summary. Turkish Central Bank Governor Serdengecti believes that while economic risks, such as from the current account deficit, are receding, the potential for political backsliding on reforms is the main threat to Turkey's economic recovery, along with potential instability in the region. The Governor, whose term ends March 14, told Ambassador he has no idea if he will be reappointed and that any governor appointed by the AK Party Government should have the ability to assert his independence and stand up to the Party and Government as needed. Advocating for market-oriented policies remains a challenge in Turkey, where neither the public nor the political system has been fully convinced of their value, even after four years of success. End Summary.

Turkey has Changed, but Public Not Convinced

12. (SBU) In a first meeting with Ambassador January 25, Central Bank Governor Sureyya Serdengecti reflected on the difficulties of his job and the risks ahead for the Turkish economy. Serdengecti, a godfather of Turkey's disinflation and economic recovery whose 5-year term ends March 14, said his biggest challenge was convincing ordinary Turks that "Turkey has really changed" and that the boom-bust and inflationary cycles of the thirty years that preceded the 2001 crisis were indeed history. Foreigners, he said, are easier to convince than Turks that the Turkish economy is a safe place for their investments.

13. (SBU) This public attitude put politicians in a difficult position. On the one hand, bringing inflation down from over 70% to 7.7% last year has bolstered the governing party's popularity. On the other, the still-dissatisfied public expects greater employment growth. Job creation means that the politicians needed to continue to implement politically costly structural reforms that foster jobs and growth but that may cut into its political popularity. In Serdengecti's opinion, the biggest risk, therefore, to Turkey's recovery is the kind of "reform fatigue" that has been seen in Latin America.

14. (SBU) The Governor was quick to point out, however, that a slowdown in the reforms would not lead to another of the catastrophic crises that Turkey has known in the past. The difference would be between relatively weak, but positive, growth and the high growth rates necessary for Turkey's living standards to approach EU averages.

Minimal Risk from Current Account

15. (SBU) Serdengeçti minimized the risk coming from a large current account deficit relative to GDP. The move to a floating exchange rate system meant that sharp adjustments in the balance of payments could lead to market turbulence but not an old style payments crisis. Also, the ongoing lengthening of the maturity of current account financing was reducing chances of an abrupt adjustment. Furthermore, the actual deficit/GDP ratio is probably lower than the current figure because a) some of the large amount of positive net errors and omissions should be included in the current account, and b) GDP will undoubtedly be revised upward. He attributed "noise in the press" about the current account and strong lira to politics: economic actors who bet against the success of the disinflation policies and kept their savings in foreign currency. As the lira strengthened, these people were losers.

16. (SBU) Other risks included increases in world energy prices, a crisis in relations with the EU, and regional political uncertainties. (The Governor was particularly concerned about the impact of an international crisis involving Iran, but also was very aware by the dangers presented by a nuclear Iran.) He thought the chances of a global emerging markets contraction were probably diminishing, and noted that the changing composition of current account financing left Turkey somewhat less exposed to external developments.

17. (SBU) Prompted by Ambassador, Serdengeçti noted that

ANKARA 00000346 002 OF 002

adverse political developments in Turkey were also a risk. He said the next parliamentary elections would be the acid test of how successful Turkey's political system has been in adapting to sound economic policies. In the past, elections had normally led to changes in government for reasons related to the inflationary economic environment. If the incumbent government were to lose in a disinflationary environment, this would confirm a fundamental instability in Turkish politics. He did not think that elections in themselves would necessarily lead to market turbulence. If markets were able to foresee the outcome beforehand, as was the case in 1999 and 2002, they should remain calm.

No Idea on Reappointment

18. (SBU) As for his personal future, Serdengeçti claimed to have no idea if the AKP would reappoint him (reftel). He suspected that the AKP is divided over the issue. While the party likes to appoint its own people to such positions, it is not always able to find qualified people within its ranks. The best economists are in Istanbul and not associated with the AKP. Although there are qualified economists in the AKP, including some at the Central Bank appointed by the AKP, their shortcoming is that they are not likely to be inclined to stand-up to the government and politicians, which any independent central banker needs to be able to do to keep his or her credibility.

POLITICIANS NOT ON BOARD FOR STABILITY AND REFORM

19. (SBU) The Ambassador noted United States support for Turkey's reforms and asked how he and the United States could best tailor messages that support continued reform. Serdengeçti expressed his appreciation for the U.S.

support, especially his good relations with the U.S. Treasury. He observed that despite the success of good policies, Turkish politicians still do not fully understand the need for stability and reform. They tend only to make the right decisions in extremis when obliged by markets. In such an environment, messages seen as applying external pressure were more likely than not to be counter-productive.

¶10. (SBU) The Governor also said he was preoccupied by recent strains in political relations between the United States and Turkey. Such difficulties are not healthy for Turkey, and are difficult to understand given everything the United States has done for Turkey since 1946. As a central banker who spends 50% of his time on public relations, he said he has an understanding of what it like to be unpopular and the difficulty of changing public attitudes. The Turkish public has, he said, a short memory, which means it is necessary to take every opportunity to remind people of what the United States has done for Turkey. Ambassador agreed that this was a concern and a very difficult problem. He said it was also important to be seen as listening to and hearing the concerns of others, even if there was not necessarily agreement on how to deal with those concerns.

WILSON